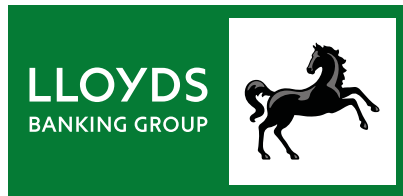




ACCOUNTING FOR  
**SUSTAINABILITY**

## SETTING SECTOR-LEVEL TARGETS

**Practical example: Lloyds Banking Group**





## WHAT

Lloyds Banking Group is a financial services provider with more than 27 million customers and a strong presence across the UK.

We have set several ambitions across our own operations, supply chain, and lending and investment activities on the path to achieving net zero by 2050 or sooner. In January 2020, we announced our interim bank ambition to reduce the carbon emissions we finance – our financed emissions – by more than 50% by 2030. In April 2021, we became a founding member of the Net-Zero Banking Alliance (NZBA), which requires member banks to take action to align their lending and investment portfolios with net zero pathways.

In support of our bank's financed emissions ambition and our NZBA membership, we have set sector targets covering our customers' scope 1 and 2 emissions, with some targets also covering scope 3. Our sector targets outline a percentage reduction in our financed emissions, with the exception being thermal coal, where we have set a commitment to exit.<sup>1</sup>

Our sectoral targets are guided by scenarios from either the UK Climate Change Committee (CCC) or the International Energy Agency (IEA).

1. For more information about our work to exit the thermal coal sector while supporting continuity in the UK's energy supply, see our [Sustainability Report 2023](#).

Practical example: Lloyds Banking Group

## Table 1: Lloyds' sector targets

Summarized from Lloyds Banking Group Sustainability Metrics Basis of Reporting, 2023.

Sector	Scopes covered*	Scenario (see definitions in HOW section)	Target type	Interim target (baseline year)
<b>Sector targets announced in 2021 and 2022</b>				
1) Power generation	Scope 1 and 2 (corporate utilities) Scope 1 (project finance)	IEA NZE 2050 (adjusted to create OECD-specific scenario)	Intensity-based	81% by 2030 (2020)
2) Thermal coal	n/a – full exit**	n/a	n/a	n/a
3) Oil and gas	Scope 1, 2 and 3	IEA NZE 2050	Absolute emissions	50% by 2030 (2019)
4) Retail motor	Scope 1 and 2	CCC BNZP	Intensity-based	More than 50% by 2030 (2018)
5) Automotive original equipment manufacturers	Scope 1 and 2 (manufacturing) Scope 3 (use of sold vehicles)	IEA NZE 2050	Intensity-based	47% by 2030 (2020)
6) Transport – aviation	Scope 1, 2 and 3	IEA ETP 2020	Intensity-based	31% by 2030 (2019)
7) UK mortgages	Scope 1 and 2	CCC BNZP	Intensity-based	41% by 2030 (2020)
<b>Sector targets added in February 2024</b>				
8) Road passenger transport	Scope 1, 2 and 3	CCC BNZP	Intensity-based	49% by 2030 (2019)
9) Commercial and residential real estate	Scope 1 and 2 Scope 3 ( <a href="#">GHG Protocol category 13 – downstream leased assets</a> )	CCC BNZP	Intensity-based	48% by 2030 (2021)
10) Agriculture	Scope 1 and 2	CCC BNZP	Absolute***	25% by 2030 (2021)

\* For more detail about the scopes and the percentage of lending covered please see our [Sustainability Metrics Basis of Reporting](#).

\*\* We achieved our target to fully exit thermal coal power in the UK by 2023. We have set a target to fully exit all entities that operate thermal coal facilities by 2030.

\*\*\* The poor data landscape in this sector means we cannot currently track emission reductions as a consequence of our actions. At present, we express our target in terms of absolute emission reductions. In order to set a future intensity target we require improvements to internal and external data capture sources to be delivered. We are investing in our own data capabilities to help address some of these data challenges do this but this will take time. [Sustainability Report 2023](#).

# WHY

Our purpose is [Helping Britain Prosper](#). Core to our purpose and strategy is our recognition of the important role we play in creating a more sustainable and inclusive future for people and businesses in the UK, by shaping finance as a force for good.

“By focusing on Helping Britain Prosper, we aim to deliver sustainable growth and returns. Guided by our Group strategy, we are focusing on areas where we can have a bigger impact.”

[Sustainability Report 2023](#)

As the UK’s largest financial services provider, we have key opportunities to support the transition of our most carbon-intensive sectors in order to meet our net zero ambitions. We aim to build on our scale and position to deliver long-term and profitable growth while making a meaningful and positive difference for all stakeholders.

Through our membership of the NZBA, we committed to develop sector-based 2030 emissions reduction targets for our most carbon-intensive sectors.

## The NZBA Commitment Statement

The [Commitment Statement](#) is a pre-requisite for joining the NZBA, and is signed by a bank’s CEO. All banks that have signed the commitment will:

- **Transition** the operational and attributable greenhouse gas (GHG) emissions from their lending and investment portfolios to align with pathways to net zero by 2050 or sooner.
- **Within 18 months** of joining, set targets for 2030 or sooner and a 2050 target, with intermediary targets to be set every 5 years from 2030 onwards.
- **Banks’ first 2030 targets** will focus on priority sectors where the bank can have the most significant impact, ie the most GHG-intensive sectors within their portfolios, with further sector targets to be set within 36 months.
- **Annually publish** absolute emissions and emissions intensity in line with best practice and within a year of setting targets, disclose progress against a board-level reviewed transition strategy setting out proposed actions and climate-related sectoral policies.
- **Take a robust approach** to the role of offsets in transition plans.

[Extract from the NZBA webpage on the Commitment Statement](#)

# HOW

Our sector targets support our bank's ambition on financed emissions. Given the strategic importance of our sustainability ambitions and commitments in managing the impacts arising from climate change and broader social issues, our group governance structure provides clear oversight and ownership of our sustainability strategy and management of risks and opportunities.

Once we have followed the steps for developing sector-level targets as set out in this section, they are presented and approved – alongside the identified strategic levers to support business delivery against the targets – at the divisional and functional-level climate and sustainability steering groups and committees. The targets will then be approved by the group net zero committee and responsible business committee and, ultimately, the group board.

- Our **group net zero committee** (group executive level) provides direction and oversees our environmental sustainability strategy. It also has oversight over how we approach our external environmental commitments and targets.

- Our **responsible business committee** (board level) oversees our sustainability strategy and sustainability-related responsibilities.

We have used a consistent approach for setting the sector-level targets, and we intend to follow the same approach when developing further sector-level targets.

Our target-setting approach for financed emissions involves four key elements:

1. Sector selection
2. Scenario and reference pathway assessment
3. Methodology and data selection
4. Determination of base year

As part of our financial planning processes, since 2021 we have projected our portfolio-level emissions to give us a forward-looking indication of our contribution to decarbonization against our interim milestone to 2030. We use this to determine whether any management intervention or portfolio realignment is needed for us to meet our target.

## Role of the finance team

We have set up a dedicated finance team to support our sustainability-related reporting.

This team is a key part of the target-setting process through building and implementing a specific set of controls for calculating and reporting on financed emissions and our lending position. These controls include reconciling figures back to the general ledger.

Once targets have been set, finance is responsible for independently aggregating and consolidating our financed emissions progress against targets on a quarterly basis to support internal and external reporting commitments.

Finance is also represented on the divisional and executive-level steering groups and committees that review, challenge and approve proposed targets.

## 1. SECTOR SELECTION

**We have prioritized setting our targets on fossil fuel sectors and other carbon-intensive sectors covering the majority of the bank's portfolio emissions in accordance with the NZBA Guidelines.**

Extract from Lloyds Banking Group's Sustainability Metrics Basis of Reporting

Sectors are selected across our three divisions:

1. Commercial Banking
2. Retail
3. Insurance, Pensions, and Investments

We applied a materiality lens to our portfolio, prioritizing the sectors where we can have the largest impact in supporting the real economy transition, while considering the availability and complexity of data.

The selection of sectors is agreed first at our divisional and functional-level climate and sustainability steering groups and committees ahead of formal approval at the group net zero committee and responsible business committee (see Figure 1):

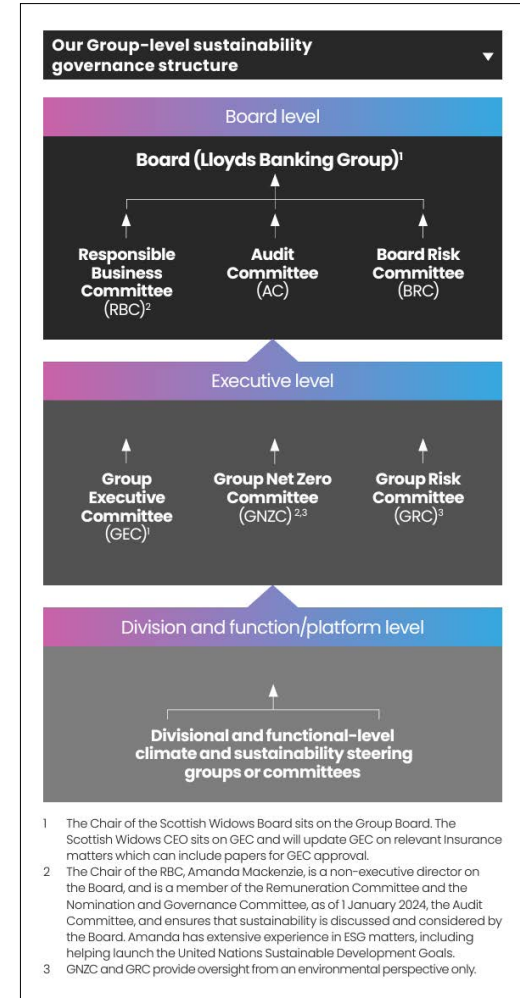


Figure 1: Our sustainability governance structure (extract from Lloyds Banking Group's [Sustainability Report 2023](#)).

## 2. SCENARIO AND REFERENCE PATHWAY ASSESSMENT

**We have used three climate scenarios and related scenario pathways as a foundation to create reference pathways. The reference pathway is calculated by rescaling the scenario pathway to our banking portfolio for the sector, such that it is equal to our NZBA target baseline emissions in the base year.**

[Extract from Lloyds Banking Group's Sustainability Metrics Basis of Reporting](#)

Our in-house environmental sustainability portfolio analytics team championed the analysis to select and apply the decarbonization pathways. To establish appropriate decarbonization pathways, we examined the make-up of our portfolio compared to the UK economy. We found that our portfolio was broadly representative, although we have a higher exposure to real estate and agriculture assets.

The three climate scenarios and related scenario pathways we used were:

1. **The International Energy Agency Net Zero Emissions 2050 (IEA NZE 2050)** – we use this scenario for sectors where our clients or their main activities have a global or regional focus.
2. **The UK Climate Change Committee's Balanced Net Zero Pathway (CCC BNZP)** – we use this scenario for UK-focused clients or customers.
3. **The IEA Energy Technology Perspectives 2020 (IEA ETP 2020)** – we use this scenario for the aviation transportation subsector specifically.



### 3. METHODOLOGY AND DATA SELECTION

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**We have continued to apply the emerging industry standard developed by the Partnership for Carbon Accounting Financials (PCAF) for measuring and disclosing financed emissions. We have used the same PCAF approach when developing baseline emissions estimates for our targets and have also used client-related targets and commitments where relevant to inform our target setting activity.**

[Extract from Lloyds Banking Group's Sustainability Metrics Basis of Reporting](#)

In the absence of comprehensive client-level data we primarily used data from the UK Office for National Statistics (ONS) and the Department for Business, Energy and Industrial Strategy (BEIS) for setting our baseline.<sup>2</sup> We have restated the baseline a few times since this original calculation in 2019 because of improvements to the quality of available data, enhanced estimation methods, and ONS and BEIS restatements. We also drew on a range of other sources, including third-party providers such as CDP and S&P.

Company-reported-data has the highest PCAF data quality score and is the preferred source of data for calculating a baseline and measuring progress against it. Typically, company-reported emissions data is more widely available for larger clients than for SMEs, who are less likely to disclose emissions data. Where company-reported data was unavailable, we used averages, such as ONS-derived factors.

2. BEIS has since been separated into three new departments: the Department for Energy Security and Net Zero, the Department for Science, Innovation and Technology, and the Department for Business and Trade.





#### 4. ASSESSMENT OF BASE YEAR

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**We select a baseline that is no more than two years from the date the target is set. This is adjusted, however, if the baseline year represents an abnormal year e.g. the baseline year for the aviation target is 2019 instead of 2020 due to the impact of the Covid-19 pandemic on travel in 2020.**

[Extract from Lloyds Banking Group's Sustainability Metrics Basis of Reporting](#)

**Establishing a baseline:** The baseline for the target is calculated following guidance in the PCAF Standard to focus on on-balance sheet drawn lending. This approach does introduce potential volatility associated with undrawn lending. At present, there is no PCAF guidance for off-balance sheet assets such as contingents or derivatives. We are engaging with PCAF on the development roadmap for future standards.



# NEXT STEPS

## ONGOING REVIEW

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We will continue to review our targets as new pathways are published, in particular for the seventh carbon budget expected in early 2025. The NZBA requires members to review their targets every five years, but we aspire to review our targets more frequently, so we can keep our targets up to date with significant developments.

## STRENGTHENING OUR APPROACH TO DATA

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Good-quality data is critical for setting sector-level targets and monitoring our progress against them. We are currently developing a cloud-based ESG data platform that will provide a 'single source of truth' for all sustainability-related data across the group. The platform will help us to strengthen our controls and ensure consistency of our data over time.





## TOP TIPS

### DEVELOP A STRONG GOVERNANCE PROCESS

Sustainability reporting is different from financial reporting, with a distinct set of expectations. For example, restatements are often found in sustainability reporting as data quality improves. Develop a strong but flexible governance process that both provides clarity where there is uncertainty and continues to provide rigour as your reporting processes and capabilities mature.

### CREATE A TARGET-SETTING APPROACH THAT SUPPORTS CHANGE

This is a fast-moving area – numbers change constantly, and data quality is a challenge. It is important to create a target-setting approach that can be adapted should something change. In time, we expect that processes will improve and changeability will settle down. Now, however, adaptation is key.

### IDENTIFY A ROBUST DATA STRATEGY

Build a data strategy for how you will source climate data, using a mix of top-down and bottom-up estimates. Use client data when it is available and reliable estimates when it is not. Draw on the external standards available – such as PCAF – to guide your data strategy. Supplement these standards with your own knowledge of specific sectors, which will help you decide what data to use and where to source it.

### BE PRAGMATIC ABOUT FILLING DATA GAPS

When obtaining data, try to identify where you can work out a missing piece based on available information. For example, if you have a company's production volumes and an emissions factor you can estimate scope 1 emissions. If you have scope 1 emissions and production data, then you can estimate an emissions factor that you can apply to other companies.

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